SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1944

No. 985

MARRS McLEAN,

Petitioner,

vs.

STATE OF TEXAS

BRIEF IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

To the Honorable the Supreme Court of the United States:

Your petitioner respectfully shows:

I

Opinions of the Courts Below

The opinion of the Court of Civil Appeals in this cause is reported in 181 S. W. 2d, 725; a copy of which is also contained in the record, pages 21-24.

II

Jurisdiction

(1) The date of the final judgment of the Supreme Court of Texas in overruling Petitioner's Motion for rehearing on his application for writ of error is December 6, 1944.

(2) The grounds of jurisdiction of this Court are set out on pages 5 to 8 of the Petition for writ of certiorari,

which are referred to and made a part hereof as fully as if recopied herein.

(3) The cases believed to sustain said jurisdiction are as follows:

Waggoner Estate v. *Wichita County*, 273 U. S. 113, 71 L. Ed. 566;

Great Northern Rwy Co. v. *Sunburst O. & R. Co.*, 287 U. S. 358-367, 77 L. Ed. 360;

Interstate Commerce Comm. v. *Cincinnati, New Orleans & T. & P. Rwy. Co.*, 167 U. S. 479, 42 L. Ed. 243-253;

Gt. Northern Rwy. v. *Merchants Elevator Co.*, 256 U. S. 285-291, 66 L. Ed. 943;

Tidal Oil Co. v. *Flanagan*, 263 U. S. 444, 68 L. Ed. 382;

Fleming v. *Fleming*, 264 U. S. 29, 68 L. Ed. 547;

Brinkerhoff-Faris Trust & Savings Co. v. *Hill*, 281 U. S. 673, 74 L. Ed. 1107;

Ferris v. *Kimble et al.*, 75 Tex. 476;

Stephens County v. *Mid Kansas Oil & Gas Co.*, 113 Tex. 160.

III

Statement of the Case

This has already been stated in the preceding petition on pages 1-5, which is hereby adopted and made a part of this brief.

IV

Specifications of Error

As a supplement to the grounds of jurisdiction, assignments of error are contained in the petition for certiorari, which are on pages 8-9, and are hereby adopted and made a part of this brief.

ARGUMENT

Summary of the Argument

POINT A. As to the jurisdiction of the Supreme Court of the United States in this cause.

The established law of the State of Texas pertaining (a) to ad valorem taxation upon segregated and severed mineral rights as real estate, and (b) pertaining to taxation of individual personal rights, has been reviewed by this Court in the case of *Waggoner Estate* v. *Wichita County, supra,* wherein the jurisdiction of this Court was sustained.

The question there presented was "that the bill assailed the tax assessed as illegal and in violation of the due process and equal protection clauses of the 14th Amendment, in that appellant's interest in the oil leases up to $718,300 of the assessed value had been erroneously treated for taxing purposes as real estate in Wichita County instead of personal property taxable in Tarrant county, where the lessor resided."

The Supreme Court of Texas in the case of *Ferris* v. *Kimble, supra,* construed Article 4676 of the then Revised Civil Statutes of Texas (which have undergone no change since that time) "Having reference to State and county taxes provides that all property, real and personal, except such as is required to be listed and assessed otherwise, shall be listed and assessed in the county where it is situated." "Article 4671 relating to the same subject makes personal property include all goods, chattels and effects, and all monies, credits, bonds and other evidences of debt owned by citizens of the State, whether the same be in or out of the State," and the Court concludes, in its decision, as follows: "Intangible personal property such as credits are taxable only at the place of residence of the owner, without

regard to where they are kept or deposited, and equally without regard to how they were earned or to the place of residence of the debtor."

The Supreme Court of Texas, in the case of *Stephens County* v. *Mid Kansas Oil & Gas Co.*, 113 Tex. 160, 254 S. W. 290, 29 A. L. R. 566, in construing the above taxation statutes on June 30th, 1923, decided the following obligation in a lease contract to be personal property and not real estate, to-wit:

> "The gas or oil in paying quantities became the property of the parties of the second part, their heirs or assigns, who were obligated to pay to the parties of the first part, their heirs or assigns, the market price of 1/10th of the gas sold, and to deliver to the parties of the first part, their heirs or assigns, ⅛th of the oil, unless they elected to pay the market price of such oil instead of making delivery thereof."

And the court in so deciding said:

TEST OF OWNERSHIP

> "*Ownership of the gas and oil in place meant having the exclusive right to possess, use, and dispose of the gas and oil. The grantors were clearly divested of the right to either possess, use, or dispose of the gas and oil in place in the lands described in the instruments here involved as soon as the instruments were executed. At the same instant, the right to possess, use, and dispose of such gas and oil in place passed to the grantees in said instruments and to their assigns.* Complete divestiture of title to the gas and oil could hardly be more clearly evinced than by the necessity for an express grant or reservation of even enough gas for domestic use in the grantors' dwellings. Dominion over a thing could not well be completer than it is in those persons who may, at their will, assign it to any other person, with or without consideration, for a time which may be forever. Sims v. Sealy, 53 Tex. Civ. App. 518, 116 S. W. 630. The fact that whoever owns the gas

> and oil, under these instruments, is subject to certain obligations to the former owners, express and implied, with regard to exploration for, and production of, the gas and oil, and with regard to the payment of royalties, in no wise reinvests the former owners with title. Nor does the possibility of future reversions accomplish present reinvestitures of title in the former owners." (Emphasis ours.)

The opinion in that case was construed by this Court in the case of *Waggoner* v. *Wichita County*, *supra*, in which the distinction was clearly marked between a lease that reserved an interest in the oil in place and one, as in the *Stephens County* case, which gave the lessee the option to pay the stipulated royalties in oil or cash, in that part of the opinion which reads as follows:

> "The case of Stephens County v. Mid Kansas Oil & Gas Co., supra, is relied upon by appellants, but in that case the lease, in other respects similar to those now under consideration, provided that the lessee at his option could pay the stipulated royalties in oil or cash. *It thus conferred on the lessee the essence of ownership: possession, with unrestricted power of appropriation and disposal of the oil.* The lessee was therefore properly fixed as the owner." (Emphasis ours.)

It will be noted that it was after the decision in the *Stevens* case that the contract was entered into between petitioner and the Yount-Lee Oil Company, which decision, by implication of law, was written into and made a part of the contract.

In the case of *Standard Oil & Gas Co.* v. *Terrell*, 183 S.W. 2d 743, it is held:

> "The laws which subsist at the time and place of the making of the contract and where it is to be performed enter into and form a part of it as if they were expressly referred to or incorporated in its terms.

> Smith v. Elliott & Deats, 29 Tex. 201; Kerr v. Gallaway, 94 Tex. 641; McCracken v. Hayward, 2 Howard 612, 11 L. Ed. 307."

In the recent Texas case of *Quintana Petroleum Company* v. *Commissioners of Internal Revenue*, by the Court of Appeals, 5th Circuit, June 27th, 1944, reported in 143 Fed. Rep. 2d series, 588, it is held:

> "The obligation of the taxpayer to pay 1/4th of the net proceeds arising from its operation arose out of a personal covenant. Such obligation vested no interest in the payee in the oil and gas in place, and entitled the payee to no percentage depletion on the amount received. The taxpayer's title to the oil and gas in place was unaffected thereby. This it recognized, for it claimed (and was allowed) percentage depletion on the gross income from production without deduction for net-profit payments.
>
> "An outright assignment is a sale, not a sub-lease. Net-profit payments are payments on the purchase price. As capital investments they may not be treated as business expenses or as rentals or as royalties. Cf. Commissioner v. Rowan Drilling Co., 5 Cir. 130 F. 2d 62."

In the case of *Great Northern Rwy. Co.* v. *Sunburst Oil & Refining Co.*, 77 L. Ed. 360, *supra*, it was held, as reflected by head-note # 2:

> "A carrier and shipper are presumed to have bargained with each other on the basis of existing law, including the judicial construction placed on a statute."

The tax authorities and the Courts of Texas as agents of the State are required by the 14th Amendment of the national Constitution to treat all citizens alike in their rights of contract.

As said in the case of *Great Northern Rwy. Co.* v. *Sunburst Oil & Refining Co., supra:*

> "Adherence to precedent as establishing a governing rule for the past in respect of the meaning of a statute is said to be a denial of due process when coupled with the declaration of an intention to refuse to adhere to it in adjudicating any controversies growing out of the transactions of the future."

In that case, involving a contract between a carrier and a shipper, it was said:

> "Carrier and shipper would be presumed to bargain with each other on the basis of existing law. Coombes v. Getz, 285 U. S. 434, 76 L. Ed. 866, 52 S.C.T. 435."

And although the petitioner in that case first asserted its federal right in motion for rehearing, of the equal protection of the law, by the failure of the Supreme Court of Montana to adhere to its former decision under which the contract was made, nevertheless it was held that it was timely raised, as said by the Court in the following language:

> "The second (referring to the above constitutional right) is a challenge to the constitutional validity of the ruling in this case whereby the statute is adjudged to mean one thing for some cases and another thing for others. This latter objection the petitioner could not make in advance of the event."

The Court of Civil Appeals in the instant case erroneously bases its decision on the case of *Sheffield* v. *Hogg*, 77 S.W. 2d 1021, dated December 31, 1934. Petitioner's assignment of said leases to the Yount-Lee Oil Co. was made long prior thereto, on to-wit, March 18, 1931, under the law as it then stood—as announced in the case of *Stephens County* v. *Mid-Kansas Oil & Gas Co.*, which was decided

June 30, 1923, and was so interpreted by this Court in the case of *Waggoner Estate* v. *Wichita County, et al.*, in its decision dated January 3, 1927. If the decision in the case of *Sheffield* v. *Hogg, supra*, by its application of the common law or the construction of the statutory law of the State of Texas, has changed the law as it stood at the time of petitioner's assignment of said leases to the Yount-Lee Oil Company, *such changes could not be given the retroactive effect of so altering said assignment and conveyance, by petitioner to the said Yount-Lee Oil Company, to the enormous extent of reinvesting in McLean the title to real estate which, by said assignment and conveyance, he had invested in the Yount-Lee Oil Company—the grantor of the Stanolind Oil & Gas Company.* However, the decision in the case of *Sheffield v. Hogg, supra, neither made nor indicated any change of the law as announced in the case of Stephens County* v. *Mid-Kansas Oil & Gas Co.*, because, as shown by the provisions in the leases copied in the opinion, *the lessors retained 1/8th of the oil, in kind, to be delivered to them as a royalty when produced.*

It was the same type of lease construed in *Waggoner's* case. This is shown by the announcement in the opinion as follows: "The real question in this case is whether a royalty interest under an ordinary oil and gas lease, is a taxable interest in real estate, and by expression 'ordinary oil and gas lease' *is meant any one of the several forms of contract which gives to the lessee the exclusive dominion and control of the oil and gas in place in the ground and provides for the delivery of a fractional part of the oil, after it is produced, to the lessor.*" The facts of the case did not involve the obligation of payment in money, based upon a percentage of the gross production of oil as a consideration for the conveyance of the entire estate in the oil, without reservation of even a lien thereon to secure said money obligation. It is therefore obviously apparent that

that part of said opinion is pure dictum, which might be claimed to include a covenant as a consideration to pay in money for the assignment of the leases based upon a percentage of the oil to be produced, and had no effect upon the law as it stood—amounting only to the expression by the Court, as a law commentator, upon "clauses in leases not actually before it." *Sheppard* v. *Stanolind Oil & Gas Co.*, 125 S.W. 2d 649. (Italics ours.)

The opinion of the Court of Civil Appeals in this case says:

> "Appellant does not undertake to urge that the law as it existed at the time the transfer was drawn up has been changed by the holding in Sheffield v. Hogg, supra, and to assert any rights to a corresponding change in construing said instrument by reason of such change."

Here is a plain indication that the *Sheffield* v. *Hogg* case had changed the law several years after the contract in question was made, and that the Petitioner was not asserting "any rights to a corresponding change in construing said instrument by reason of such change."

It is manifest that Petitioner could not anticipate that the court would construe the *Hogg* case as having changed the law under which his contract was made; nor could he anticipate that if the law was changed by that case there was any duty at that stage of the proceedings laid upon him to assert his constitutional rights that such change could not retroactively annul and destroy his lawfully invested rights under his contract of March 18, 1931.

When such holding was made as a predicate to destroy his contractual rights, he laid the predicate by timely motions by asserting that such action was in violation of the Federal Constitution, which, as held by the United States Supreme Court, in the *Sunburst* case, was "timely raised," and "a challenge to the constitutional validity of the ruling

in this case, whereby the statute is adjudged to mean one thing for some cases and another thing for others. This latter objection the Petitioner could not make in advance of the event." (See page 17, *supra.*)

POINT B. Argument and authorities in support of the contention that the assignment of the leases, as made by its terms and the consideration therein expressed (including the obligation of $2,000,000.00 to be paid from the percentage of the gross oil, when produced), is to be construed in the light of the surrounding circumstances together with the expressed oral intention by the parties of the meaning of its terms, and their acts under the contract consistent with such meaning, and inconsistent with any other meaning.

The Court of Civil Appeals in its opinion, which opinion has been presumptively adopted by the Supreme Court of Texas in refusing writ of error, has erred in denying in this case that the above contention is the law of Texas. The opinion shows the undisputed facts on which the court acted as follows:

> "The court expressly found that the appellant and the attorney for the transferee carefully worded the transfer with the intention of making the oil-payment personal property so as to place the burden on the transferee of liability for ad valorem taxes on the full 75%, to the end that appellant should not have to pay any part of the ad valorem taxes thereon. Also, it was undisputed that the Yount-Lee paid all ad valorem taxes on the 75% so long as it continued to own same, as well as paid 75% of the production tax. Thereafter, on July 31, 1935, the Yount-Lee disposed of the working interest in said leases, and on the same day the Stanolind acquired it. And the Stanolind continued to pay taxes in the same way as the Yount-Lee had done, until the year 1939. The Stanolind then, for the first time, contended that the unpaid portion of the oil-payment obligation was, for taxation purposes, an

> interest in land, and declined to pay ad valorem taxes on so much of the 75% as represented the oil-payment."

And the court's opinion upon the above facts in connection with the assignment, held:

> "It is therefore immaterial what the purpose and intention of the parties to the transfer were at the time they drafted said transfer, except as the same is expressed by the terms of said transfer."

And further:

> "If in fact the entire working-interest, to the extent of 75% of the mineral estate, passed by the transfer to the Yount-Lee, as the parties intended and supposed, then, necessarily, the oil-payment obligation would be personal property. But the intentions of parties cannot change the character of an estate which is fixed by law, and which they by their acts create."

The opinion then follows with the erroneous assumption from said assignment and the facts and circumstances above related that "when the appellant (petitioner) retained the right to share in the oil produced to the extent of 12½% thereof or its money equivalent he retained the right to share in the profits — in the profits a prendre out of the 75% working interest. Such right is an interest in land." It is obvious that such assumption has no foundation in the facts as the assignment, by its terms and the meaning placed thereon by the parties, shows affirmatively to the contrary, to-wit, that McLean conveyed the entire estate of 75% in the oil in place, and as a part of the consideration therefor Yount-Lee Oil Co., covenanted to pay $2,000,000.00 based upon a percentage of 12½% of the gross production of the oil, if and when produced, and orally agreed that such obligation of payment should be personal property.

The Commission of Appeals in *State National Bank* v. *Morgan*, 143 S.W. 2d 757, held that in construing the language of leases bearing on an oil payment as bonus, the parol evidence is admissible and competent which discloses the intention of the parties.

In the case of *Humble Oil & Refining Co.* v. *Reclamation Company*, 58 S.W. 2d 1084, the Court said:

> "Both parties contend, in their briefs, that this court should adopt the interpretation of the contract placed thereon by the parties (though they differ in this case as to what that intention was). This rule has application though the contract is not ambiguous."

In the case of *Rio Bravo Oil Company* v. *Weed*, 52 S. W. 2d 1086, Judge Leddy for the Commission of Appeals said:

> "It is well said by the Court in the case of Livingston Oil Corporation v. Waggoner (Tex. Civ. App.) 273 S. W. 903, 906: 'It is to be assumed that parties to a contract know best what was meant by its terms, and are the less liable to be mistaken as to its intention; that each party is alert to protect his own interest and to insist on his rights; and that whatever is done by the parties during the period of the performance of the contract is done under its terms as they understood and intended it to be'."

It is held in the recent case of *Humble Oil & Refining Co.* v. *Ellison* (Smedley, Comm. of App., opinion adopted), 132 S. W. 2d 395, that the written language in a conveyance under the statute of frauds can be explained by parol, if there is an ambiguity in the language of the instrument, or when applied to the subject matter.

The Supreme Court of Texas in the case of *Lone Star Gas Co.* v. *Ray Gas Co.*, 164 S. W. 2d 508, held:

> "that the practical construction placed upon a contract by the parties themselves constituted the high-

est evidence of their intention that whatever was done by them in the performance of the contract was done under its terms as they understood and intended same should be done."

In the case of *Sacramento Nav. Co.* v. *Salz,* 71 L. Ed. U. S. Supp. Ct. 663, it was held:

"But a contract includes not only the promises set forth in express words, but in addition all such implied provisions as are indispensable to effectuate the intention of the parties and as arise from the language of the contract and the circumstances under which it was made."

Conclusion.

Since taxes on land cannot be enforced against any one except the owner, the test of what constitutes ownership is the only logical inquiry.

This has been authoritatively settled in Texas by its highest court in the Stephens county case, quoted above. It is an exhaustive opinion. The Court said:

"The Honorable Court of Civil Appeals has certified to this Court *the single question, whether the appellee acquired under the above mentioned instrument, such interest or such estates in land as were subject to separate taxation.* The certificate recites that numerous suits involving the question are pending, and that its *authoritative determination is of the utmost importance.*

"*Looking to the manifest intent of the parties,* we do not think it difficult to arrive at a correct answer to the questions. *The subject matter of each contract was oil and gas in place. The principal consideration was royalties dependent upon the marketing of the gas and oil*" (Emphasis added).

In this outstanding case the Court cites its own previous decisions on the point, and decisions of Pennsylvania,

Kentucky, New Jersey, Illinois, California and Louisiana —the general law of oil and gas of these producing states. The Stephens County case was cited and reaffirmed by the Texas Supreme Court in *Humphries-Mexia Co.* v. *Gammon,* 254 S. W. 296; *Texas Company* v. *Davis,* 254 S. W. 304, and numerous other cases, without dissent or qualification.

In the last named case the court, speaking through the same judge, said (p. 309):

> "Our object is to announce a rule which is truly consonant with the real intent of the contracting parties."

Such is the declared law of Texas in the decisions of its highest courts. The test so laid down was as above quoted fully approved in Waggoner's appeal.

In other words, Waggoner's jurisdictional ground rested upon his averment of fact that he retained no title to the minerals in place but was nevertheless taxed as a realty owner, when in fact he was not in such class but was in the class of realty owner of minerals in place—unlike Hill et al., in the Stephens County case. Their contracts were totally different as to investiture of title to the minerals in place.

If Waggoner's facts had been as the facts considered in the Stevens case, his appeal, under Justice Stone's opinion, would manifestly have been upheld by the court.

A tax on land is not a tax against a person. It is a tax *in rem.*

The right of ownership in land is a right of private contract with which the agencies of the state have no concern except to enforce and protect.

Ad valorem taxes concern only the owner who is interested to prevent a tax lien being foreclosed against his property. That is why the court erred in refusing to hold

these parties to the terms of their contract. The state can make no contract for them at variance with their intentions; nor can it make a non-owner pay an owner's tax.

In this case it sued both McLean, who did not own the land, and the Stanolind Company which did own it. The State's agencies levied the tax against a non owner, and by judicial process ordered the sheriff to collect the taxes due by the owner against McLean, who ceased to be the owner in 1931, when he sold and conveyed to Yount who, in turn, four years later, sold and conveyed it to the Stanolind.

Such arbitrary action by the agents of the State in this case sets at naught the safe-guards of the Federal Constitution.

It is, therefore, respectfully submitted that this case is one calling for the exercise by this Court of its supervisory power, by granting a writ of certiorari and thereafter reviewing and reversing said decision.

Respectfully submitted,

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